The Quaker Oats Company Annual Report 1972

QUAKER

The Faces of Quaker

QUAKER

These are the faces of Quaker.

Of customers of all ages.
Families.
Boys and girls, men and women.
People young and old.
All races and nationalities
Around the world.
Even family pets.

Of products
Quaker products.
Nutritious oats and other cereals.
But not only these.
Other foods for good health and nutrition
All foods to enjoy.
Toys for young children
To play with and learn with.
Wholesome meals for family pets
To keep them lively and healthy.
Embroidery, stitchery, yarn
For creativity in leisure time.
Even chemicals
Helping provide so much
We work, play and live with.

Of the Quaker Man
Both old and new.
Behind his face, what doesn't show
But yet abides.
Quality.
Value.
Imagination.
Honesty.
And Quaker employees
Who make it all work.
Thus is dimension added to

The faces of Quaker.

Some Puss 'n Boots and a lot of love. . .enough to make any cat purr with pleasure.

Quaker's fortified cereals for the whole family. . .high protein Life and King Vitaman, which provides 100 percent of the daily requirements of vitamins and iron.

The Fisher-Price Play Family Airport. . . just the ticket for the pre-schooler who wants to run his own airline.

Traditional Quaker Oats . . . the natural and nutritious hot cereal that's been a family favorite around the world for almost a century.

Celeste frozen Ravioli Dinner . . . newest, boil-in-the-bag convenience that preserves the flavor of "the old family recipe."

Quaker's new Needlecraft Division . . . art stitchery for creative people, and a new growth business for Quaker.

The Marx Big Wheel . . . the envy of every youngster on the block.

The Girl Scouts of America raise millions of dollars a year by selling cookies, and Quaker's Burry Division is one of their largest suppliers.

Ken-L Ration Cheese-Flavored Burger, just one of a complete line of balanced meals for dogs of all sizes.

In Mexico, it's Carlos V, one of many bar and beverage chocolates made by Quaker's Fabrica de Chocolates la Azteca.

A quick brunch from Aunt Jemima . . . convenient frozen french toast and delicious Aunt Jemima syrup.

All Canadians know Muffets, one of that country's leading ready-to-eat cereals.

Just add hot water and stir for a piping hot, nutritious bowl of Instant Quaker Oatmeal.

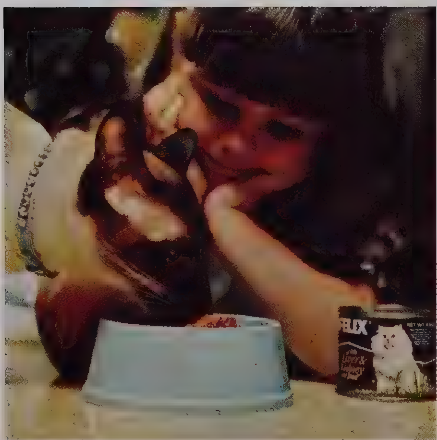
Delicious crêpes, memorable decor . . . dining out at The Magic Pan is a delightful and unique experience.

The best way to start the day is with a breakfast of juice, cereal, milk and toast. Quaker makes cereals that children love.

The Play Family Houseboat . . .one of the quality, durable, Fisher-Price hand-me-down toys. It floats!

In Quebec they call them Gauffres, in the U.S. they're frozen waffles. Either way, they're popular Aunt Jemima favorites for luncheon as well as breakfast.

Nothing beats home-made tortillas, and nothing beats Quaker's Masa Harina for making them.



In the United Kingdom, favored felines feast on Felix cat food.

Willy Wonka's Super Skrunch . . . an American favorite in less than a year.


COOKS IN
MINUTE
BURGER

Thousands o

Year Ended June 30	**1972**	1971	**% (D**
Net sales	**$771,159**	$678,732	
Income before income taxes	**67,790**	58,641	
Income before extraordinary charge	**34,244**	30,065	
Extraordinary charge	—	5,886	
Net income	**34,244**	24,179	
Preferred dividends declared	**484**	490	
Common dividends declared	**13,006**	12,636	

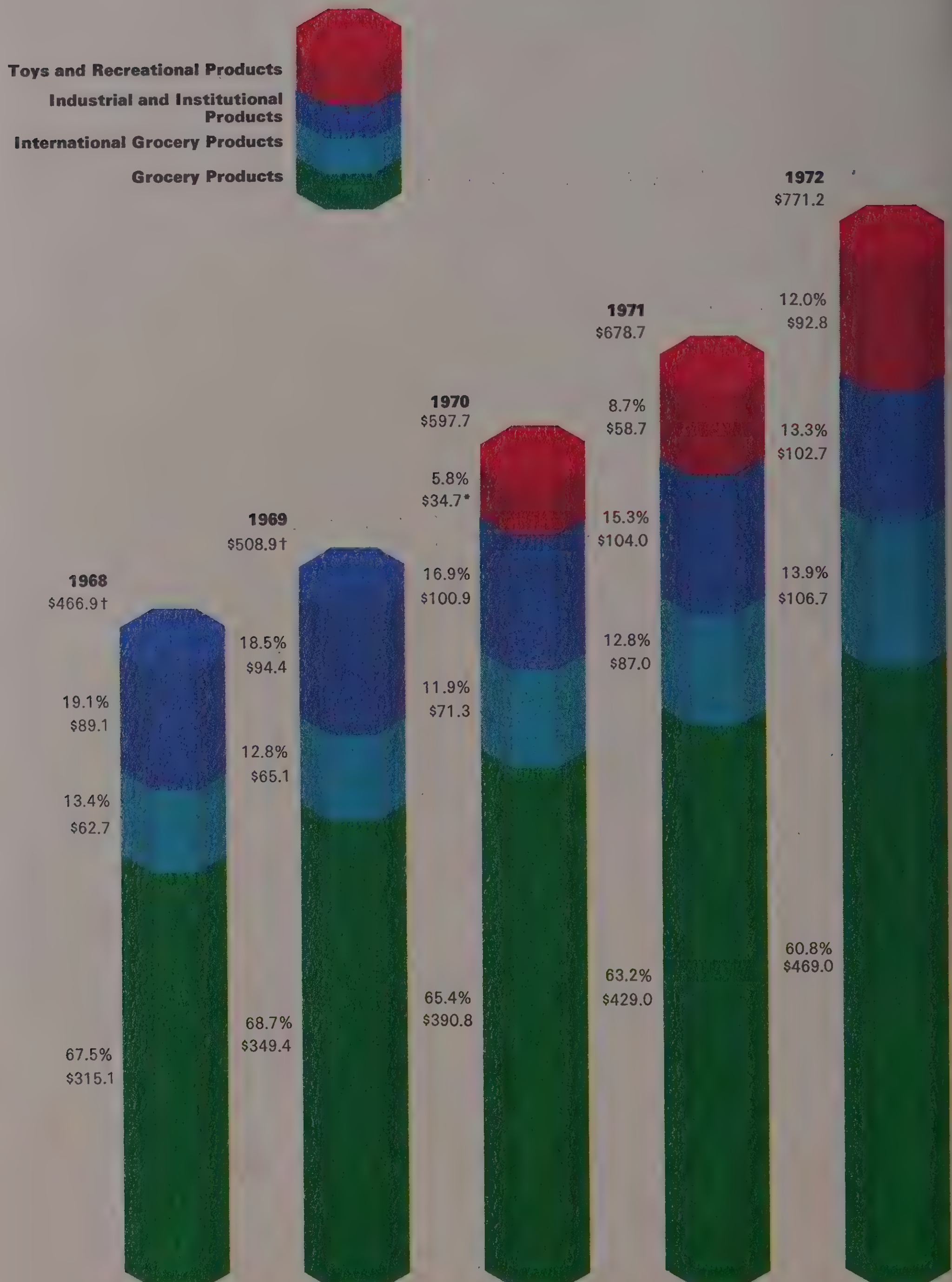
Per Comm

Income before extraordinary charge	**$2.65**	$2.34	
Extraordinary charge	—	.47	
Net income	**2.65**	1.87	

Consolidated Sales Growth by Operating Groups

Sales in Millions of Dollars

†Adjusted to Exclude Divested Businesses
*Ten Months After Acquisition by Quaker



To all Quaker Shareholders

New records in sales and earnings were established in fiscal 1972, a year in which we made further progress in broadening our base as a marketer of consumer products and specialty chemicals. Sales advanced 13.6 percent to $771,159,000, while per-share earnings were up 13.2 percent to $2.65.

For the five years ending June 30, 1972, per-share earnings before extraordinary items increased an average of 12 percent per year, again meeting our objective of at least 10 percent average annual improvement over any five-year period.

Technical research and development in the year continued to receive major emphasis, and expenditures were up 19.4 percent compared with fiscal 1971. We made further progress in increasing the proportion of our assets invested in areas that have above-average potential for Quaker. Return on shareholders' equity improved from 13.1 percent to 13.4 percent.

Operating Performance The largest single factor in the earnings improvement, compared with last year, was the excellent performance of the Fisher-Price Toys Division — a major example of the importance of a broadened base. At the same time, the long-established grocery products brands continued to be the largest source of earnings. Earnings of the Grocery Products Group, which includes Canada, were little changed from last year, as explained on page 8 of this report.

The Grocery Products sales increase was aided by advances in pet foods, mixes, syrup and corn products. Frozen food sales, supported by heavy marketing investments, almost doubled. Sales of both hot and ready-to-eat cereals were about even with last year.

The Quaker Oats Company of Canada Limited achieved excellent improvement in sales and earnings.

International Grocery Products showed significant sales progress during the year, particularly in Europe and Mexico, but operating earnings were level — reflecting both new-product underwriting and difficult economic conditions in South America. Strong emphasis is being placed on further developing our business opportunities in Europe.

The Burry Division turned in its second consecutive year of improved performance.

Strength in European chemical markets helped offset some softness early in the year in the U.S., and contributed to another year of satisfactory performance by the Chemicals Division.

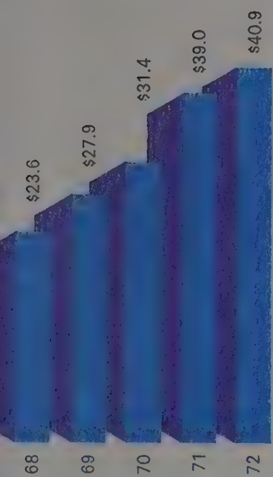
Acquisitions Two important acquisitions were completed recently. Each is a good example of the type of growth we are seeking as we expand our base in consumer products.

Louis Marx & Co., Inc. — a leading manufacturer of children's riding toys, games, trains and other toys — was purchased for about $51 million cash. Approximately $37 million was paid for Marx's world-wide net operating assets, including normal working capital requirements, and $14 million for seasonally expanded working capital. This purchase was effected on June 30, the last day of our fiscal year, and Marx sales and earnings are not included in our operating results for the 1972 fiscal year. Marx had world-wide sales of approximately $67 million in calendar 1971.

On July 20, 1972 — subsequent to the close of the fiscal year — we completed a merger with Needlecraft Corporation of America, in return for 424,813 authorized but unissued Quaker common shares. The Needlecraft group of operating companies is engaged in yarn processing and the art needlecraft kit and mail-order businesses. In its fiscal year ending April 30, 1972, Needlecraft had sales of about $24 million.

Marx complements our existing toy business by offering different types of toys and games for children of broader age groups. Needlecraft allows us to participate in the expanding field of creative crafts for leisure-time use by adults and older children. Both firms provide opportunities in new areas with significant growth potential for Quaker.

Capital Expenditure
Millions of Dollars



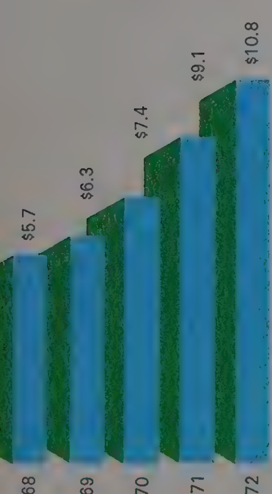
Investment for Future Growth We are continuing to invest substantial amounts each year to support future growth of the business. Excluding acquisitions, capital expenditures in fiscal 1972 were about $41 million, and have increased at an average annual rate of about 14 percent during the past five years. Principal spending last year was for new facilities to manufacture toys, pet foods, frozen foods and chemicals.

In addition, substantial amounts are being invested to assure compliance with good manufacturing practices, pollution control considerations and requirements of the new Occupational Safety and Health Act.

Capital expenditures in fiscal 1973 are projected to be between $45 million and $50 million.

There were technical research expenditures of $10.8 million in fiscal 1972, for scientific and engineering research and development, the creation of new products, and quality maintenance and improvement of existing products. The figures do not include market research or plant quality control.

Technical Research
Millions of Dollars



Technical research on grocery products and chemicals is carried on primarily at the John Stuart Research Laboratories in Barrington, Illinois, with some additional studies conducted abroad. Fisher-Price toy research is carried on primarily at that Division's research center in East Aurora, New York.

We are continuing our heavy emphasis on technical research, seeking those products that will possess lasting, distinctive consumer benefits, as well as new applications of the Company's specialty chemicals.

Litigation In April, 1972, the Federal Trade Commission filed formal charges against four manufacturers of ready-to-eat cereals, including Quaker, alleging that between them they share a monopoly in the business. No conspiracy was charged. We have denied the FTC charges, which we believe are without merit.

Consumerism and Public Responsibility In prior years' annual reports, we have attempted to summarize the Company's efforts to serve consumers and meet public responsibilities. We believe leadership in these areas is important to the vitality of our business and our people, and we have tried to be involved, innovative and effective.

To ensure overview by the Board of Directors, a Public Responsibility Committee — consisting of three outside directors, the President and two other inside directors — was established. We are pleased with the critical evaluation and additional emphasis this places in an area we have long considered important. A set of Company publications describing our programs and accomplishments to date is available on request to shareholders and other interested parties.

People At year-end, there were approximately 16,900 Quaker people around the world responsible for moving our Company forward. They are a strong and proven asset for the future.

In May, Quaker people were saddened by the sudden death of Lowell W. Michael, Vice President — Engineering, at the age of 53.

In March, H. Earle Muzzy died at the age of 81. His career with Quaker spanned 46 years, including service as President and Vice Chairman of the Board. He had been retired since 1959.

Dividends In January, the Board declared a 4 percent increase in the quarterly dividend, to 26 cents a common share. This was the fifth consecutive fiscal year in which the dividend was increased.

To provide a convenient and economical service to shareholders, an Automatic Dividend Reinvestment Service was inaugurated during the year. About 10 percent of all shareholder accounts are already signed up for automatic reinvestment of Quaker dividends in Company common shares — a most gratifying response.

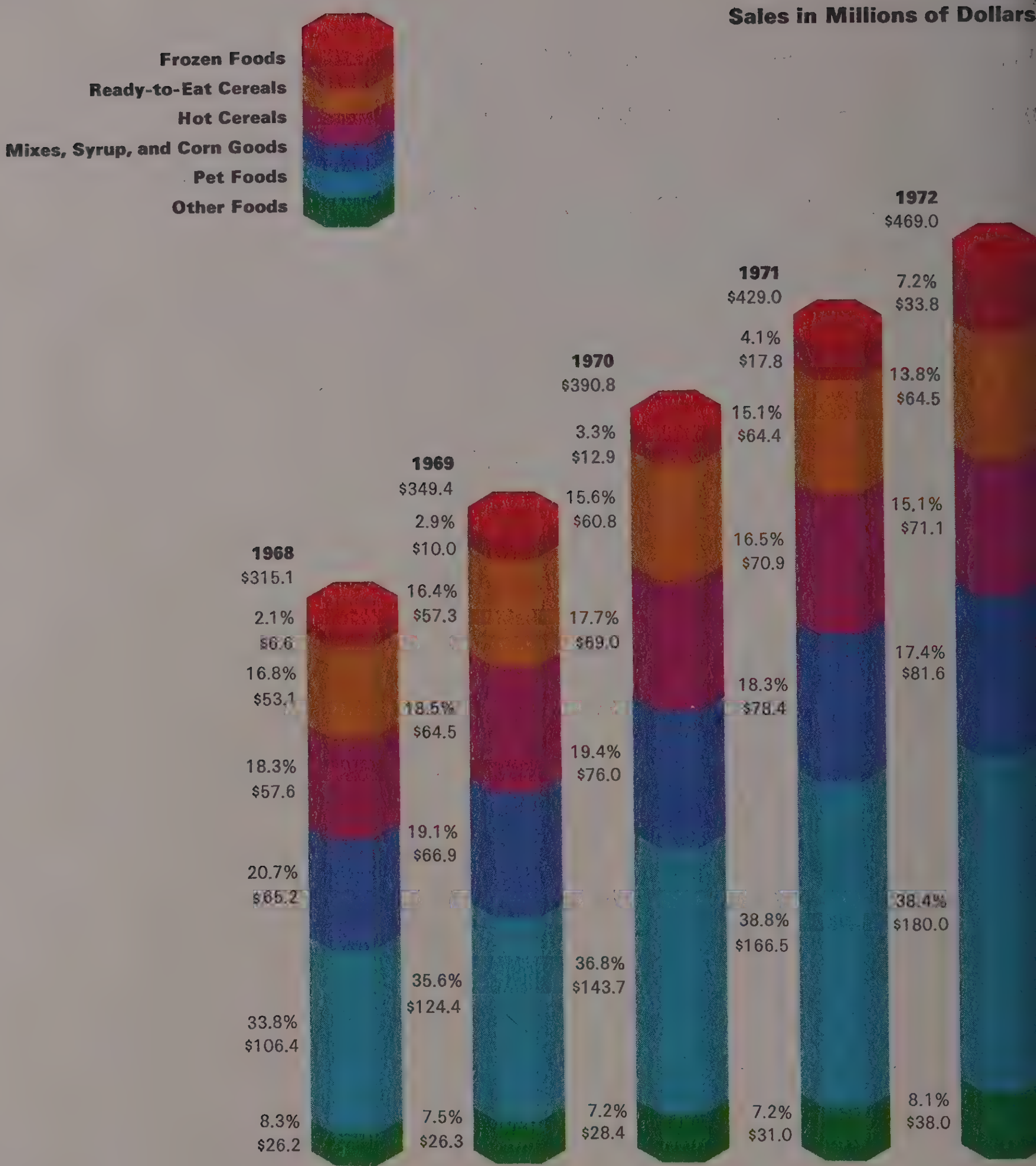
A Look Ahead Changing trends in consumer needs and desires, along with rapid technological advances, will be major factors in consumer products marketing in the years ahead. For some time we have recognized the significance of the decreasing percentage of the consumer dollar spent on food and the resulting increased percentage available for purchases in other areas.

To achieve optimum growth, we are concentrating new resources on the dynamic parts of the food business and on other businesses with growth rates superior to food. Considerable progress has been made in this direction in recent years. We are optimistic about our future.

Robert D. Stuart Jr.

Robert D. Stuart, Jr.
President and Chief Executive Officer

September 13, 1972



Grocery Products Group

The Grocery Products Group is the largest contributor to Quaker sales and earnings. Group sales of U.S. and Canadian foods and pet foods increased 9.3 percent during the 1972 fiscal year, but operating earnings were up only slightly. Cost increases in ingredients other than grain offset favorable grain prices. Heavy marketing investments in frozen foods and candy, increased fixed costs for new production capacity, and less than satisfactory results from the motion picture

produced a year ago, *Willy Wonka and the Chocolate Factory,* also adversely affected operating earnings.

New product emphasis is on dynamic parts of the grocery products business, such as convenience pet foods and specialty frozen foods.

Cereals and Mixes Division Cereals, which the Company makes for a large and relatively stable market, were essentially level in sales.

Traditional oatmeal and the newer instant oatmeals continued as established market leaders. An Instant Oatmeal Variety Pack, containing natural and flavored products, was successfully introduced during the year. A chocolate-flavor Instant Oatmeal, however, did not sell well and has been discontinued.

Life and Cap'n Crunch brands both sold very well during the fiscal year, while King Vitaman sales declined compared with the prior year.

Aunt Jemima pancake mixes and syrup and corn products produced good sales. Quaker Instant Grits, marketed primarily in the South, grew substantially in sales. In each of these product categories, market share improved.

The Cereals and Mixes Division's product development effort is showing promise, with the expectation that new products — including two new cereals — will be introduced during 1973.

Frozen Foods Division The Frozen Foods Division markets Aunt Jemima Frozen Waffles and French Toast, as well as the expanding line of Celeste frozen Italian foods. Division sales were almost doubled in fiscal 1972, as a result of significant investment in new-product development and market expansion.

Aunt Jemima French Toast was introduced and is now in full national distribution. Aunt Jemima Cinnamon Swirl, a frozen french toast line extension, is moving into national markets.

Celeste frozen Italian specialties — previously a limited local brand — underwent considerable market expansion during fiscal 1972, and are now available in more than half the United States.

Candy Division The Company entered the U.S. candy business in fiscal 1972, on the premise that distinctive new products and Quaker experience in marketing to families with children could make candy a good growth area. Two products were introduced — Willy Wonka's Super Skrunch and Willy Wonka's Peanut Butter Oompas. Considerable underwriting of this new venture helped achieve sales of $9 million.

Pet Foods Division Sales increased about 8 percent, but earnings progress of the Pet Foods Division was limited by higher raw material costs and expenses associated with new and enlarged capacity.

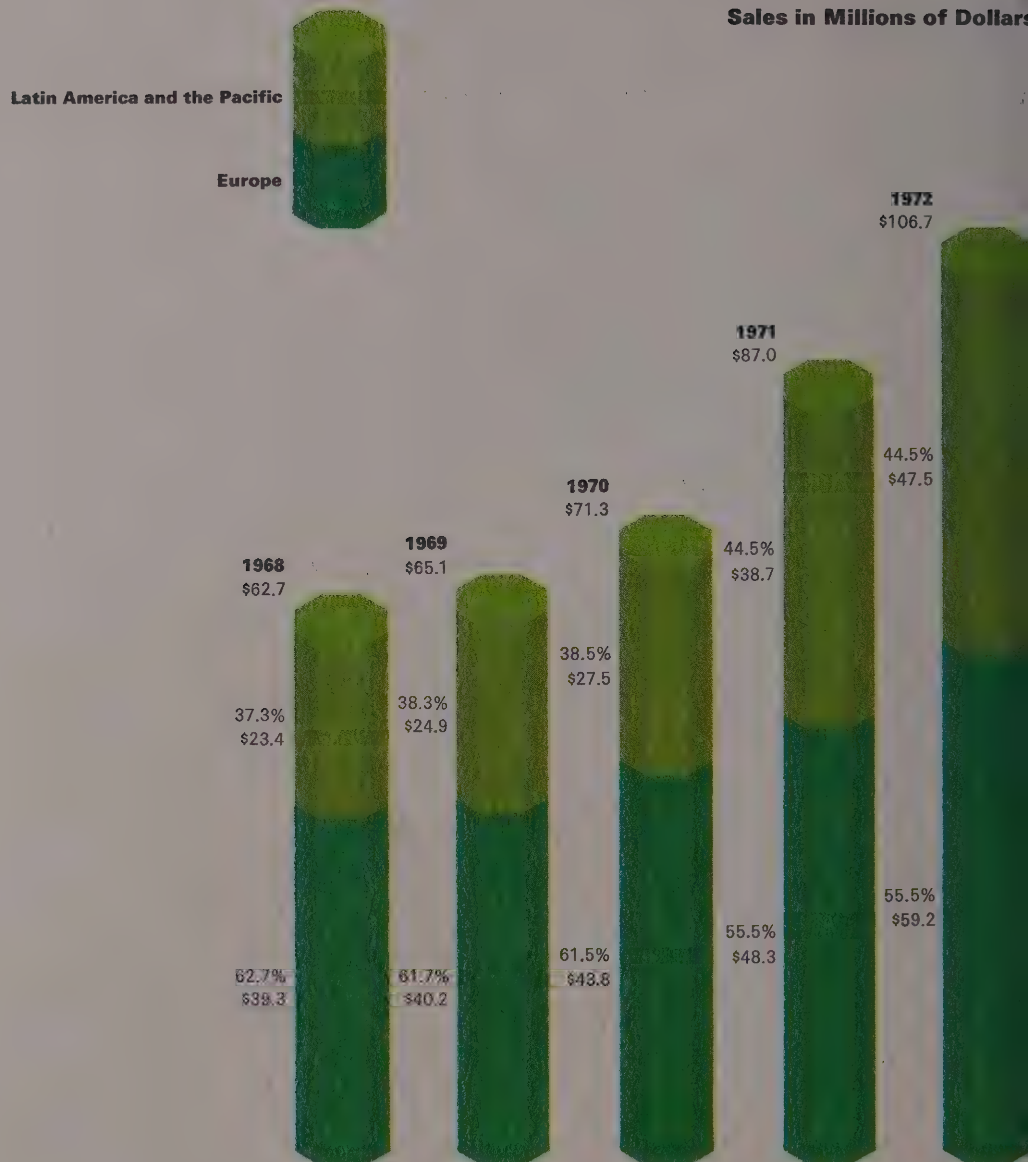
Ken-L Ration canned dog food increased dollar volume and market share despite strong competitive activity.
Dry dog food experienced a modest sales decline. Due largely to broadened marketing of Ken-L Ration Cheese-Flavored Burger, sales of the Group's semi-moist dog foods — regular and Cheese-Flavored Burger and Ken-L Ration Special Cuts — were up substantially.

Sales of Puss 'n Boots cat food were level, reflecting a realigned marketing strategy designed to concentrate on those segments of the market where Quaker is best able to compete. Two new canned products were introduced to national markets during the year.

Canada Both sales and income of The Quaker Oats Company of Canada Limited improved considerably during the 1972 fiscal year. This progress reflects improved marketing strategies for new and existing products, the successful implementation of strong cost-control programs, a consolidation of manufacturing locations, and a divisional reorganization providing autonomous management in Canada with a close interface with the related U.S. grocery products business.

The Canadian pet foods business continues strong. The Ken-L Ration, Strongheart and Society brands are selling well, and have a significant position in the market. Puss 'n Boots cat foods, extremely well established in Canada, are expected to produce further growth through new product innovation.

Aunt Jemima Frozen French Toast was introduced throughout Canada during the year, and has added to the existing strong business of Aunt Jemima Frozen Waffles.



International Grocery Products Group

International Grocery Products sales were up about 22 percent in the 1972 fiscal year, with increases in almost every country. These increases are attributable to accelerated investment in existing and new franchises in Europe, and expansion of the business in Australia — largely as the result of a pet foods acquisition.

As a result of marketing investments made in new pet food products as well as price control problems in Latin America, operating income was up only slightly from last year.

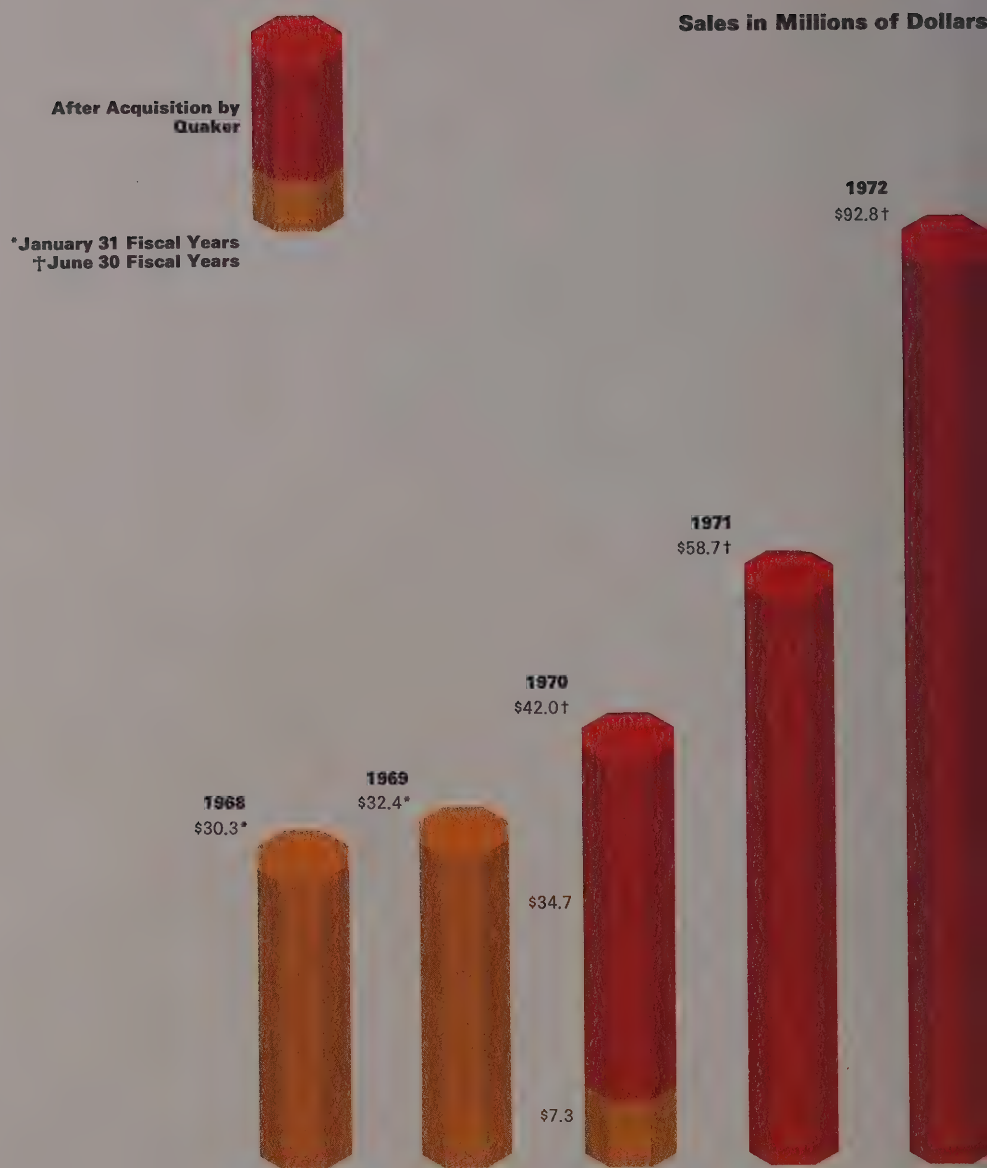
The International pet foods market shows promising growth potential, and Quaker is in a good position to participate. The cereals business is relatively stable, and provides a firm profit base that generates earnings to finance future growth.

Europe The Company has subsidiaries in the United Kingdom, Scandinavia and the Netherlands, where hot and ready-to-eat cereals and pet foods are principal products. In the United Kingdom, sales of Quaker Oats and Sugar Puffs and other ready-to-eat cereals remain stable, while sales of pet foods are increasing. Sutherlands sandwich spreads and Quaker macaroni continue to be market leaders. After successful test-marketing, new semi-moist dog foods similar to U.S. and Canadian Ken-L Ration Burger have been introduced nationally in British, Benelux and Scandinavian markets. New and expanded pet food production facilities have gone on-stream in England and Denmark.

Latin America and the Pacific In Mexico, the Company has a substantial and successful business. Fabrica de Chocolates La Azteca showed good growth, both in its large chocolate confection and beverage business and in the traditional lines of Quaker cereals and mixes.

Quaker's businesses elsewhere in Central and South America involve oat cereals, beverage mixes and corn products. In those countries with relatively stable economies and good growth opportunities, present plans are to add new products both through internal development and acquisition.

In Australia, Quaker has a small hot cereals business and an expanding pet foods business, enhanced by the acquisition announced in November of Luv Pet Foods Pty. Limited — a principal Australian pet foods manufacturer. The modest Quaker position in the marketplace improved during the year, and the combination of Luv with existing Company interests provides an opportunity to increase efficiencies and further expand market shares.



Toys and Recreational Products Group

The Fisher-Price Toys Division had an exceptionally good year, breaking prior sales and earnings records.

A sales increase from $58.7 million to $92.8 million and substantial increases in operating income contributed strongly to Quaker's results for the year. This growth was achieved despite a generally slow season for the toy industry.

The consumer's growing insistence on durable, safe and imaginative toys for young children continues to be a favorable factor for Fisher-Price. High trade acceptance was reflected in several awards presented to the Division by organizations at the wholesale and retail levels.

The Play Family School was the country's leading toy last Christmas, and other new toys were successful. Well-established staple items such as the 35-year-old Snoopy Sniffer and other Fisher-Price mainstays also sold well. Among the promising new toys introduced in February are the Play Family Airport, Play Family Houseboat, Play Desk and a line of Pick-Up-and-Peek-Puzzles.

European Growth In December, Fisher-Price Toys Limited, a newly formed British subsidiary, entered into an agreement with The Mettoy Company, Limited, a prominent British toy company, for the production of Fisher-Price toys in Swansea, Wales, and for marketing in the United Kingdom and Continental Europe. Subsequently, a small ownership position in Mettoy was purchased.

Marx/Needlecraft In fiscal 1973, Louis Marx & Co., Inc., and the Needlecraft Division — both described in the President's Letter on page 4 — will be part of the Toys and Recreational Products Group. Needlecraft provides opportunities to participate in the market for creative crafts used by adults and teenagers, while Marx adds significant toy volume in product areas new to Quaker.

Industrial and Institutional Products Group

Group sales for the 1972 fiscal year were off slightly from a year ago. Gains in the Chemicals Division and Magic Pan restaurants were offset by planned reductions in the Burry Division. Group operating income improved, reflecting primarily the Chemicals Division and continued progress in Burry.

Chemicals Division The Chemicals Division's principal products are furan chemicals — a family of specialty chemicals used in the foundry, petroleum, plastics and rubber industries. Good progress was made during the year, particularly in European markets.

Research and development has been very important to Chemicals' business success in recent years, and a number of new products and applications are the result of the concentrated R&D effort. To further expand and capitalize on the Division's R&D capability, a new 40,000 square-foot chemicals laboratory building was constructed at the Company's Barrington, Illinois, research site.

The specialty applications of furfuryl alcohol in the foundry industry were a principal factor in the Division's sales increase during 1972. The use of sand regeneration units in association with furfuryl alcohol binders contributes significantly to improving foundry economics and assists in reducing pollution.

Increased sales in Europe, reflecting the expansion of the furfuryl alcohol plant in Antwerp, Belgium, were significant. A second major furfuryl alcohol plant at Geel, Belgium, is now going on-stream. In the U.S., the first phase of a production expansion at the Belle Glade, Florida, furfural plant was completed.

Burry Division Fiscal 1972 was the second consecutive year of improved results for the Burry Division, resulting from planned changes in marketing, distribution and manufacturing strategy.

The Division manufactures branded crackers and cookies sold at wholesale and through grocery stores, and provides food service sales direction for Quaker and Burry institutional products. Burry is one of the largest bakers of Girl Scout cookies in the U.S., and is a major supplier of wafers to the ice cream specialty market.

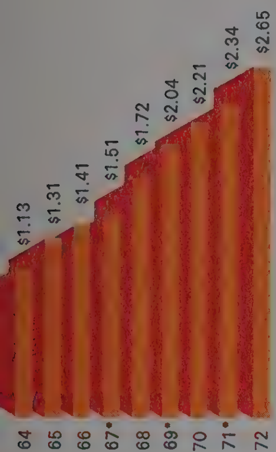
Magic Pan With seven units in operation for a full year, sales of the Company's wholly owned Magic Pan restaurants — while still modest — were substantially higher in fiscal 1972. Six more restaurants are now scheduled to be opened during fiscal 1973.

QUAKER

Financial Information

Growth in Earnings Per Share One of Quaker's financial objectives is to improve per-share earnings an average of at least 10 percent a year over any five-year period, before any extraordinary income or charge. This goal assumes that some years' per-share earnings growth will exceed 10 percent, while other years may fall below that level. Five-year averages are as follows:

Earnings Per Share
(Adjusted for stock splits)
*Excludes extraordinary item



5-Year Periods Ending June 30	5-Year Average Per-Share Earnings Improvement
1969	12.6%
1970	11.1%
1971	10.8%
1972	12.0%

The adjoining table shows actual earnings-per-share data for nine fiscal years.

Sales and Operating Income by Groups Trends for each Quaker operating group are discussed in the respective Group sections earlier in this report. Actual data is as follows:

Year Ended June 30	Millions of Dollars	
Sales	**1972**	1971
Grocery Products Group	**$469.0**	$429.0
International Grocery Products Group	**106.7**	87.0
Toys and Recreational Products Group	**92.8**	58.7
Industrial and Institutional Products Group	**102.7**	104.0
Total	**$771.2**	$678.7
Operating Income		
Grocery Products Group	**43.1**	42.5
International Grocery Products Group	**5.6**	5.5
Toys and Recreational Products Group	**20.0**	11.5
Industrial and Institutional Products Group	**5.6**	4.5
Total	**74.3**	64.0
Less interest expense (net)	**6.5**	5.4
Income before income taxes	**$ 67.8**	$ 58.6

Financing The Company has always maintained a strong, highly flexible financial position. Quaker's policy is to make aggressive use of borrowing and, at the same time, maintain the ability to take full advantage of unforeseen investment opportunities. In accord with these concepts, the Company expects its debt ratio (long-term debt to total capital) will be maintained between 25 and 35 percent.

Late in fiscal 1972, a seven-year, $40 million revolving credit-term loan facility was arranged with a group of banks to provide a source for future working capital and fixed asset requirements. Borrowings and repayments under this agreement can be made any time during the next three fiscal years, and there are no required repayments for seven years. On June 30, 1972, $37 million was borrowed in connection with the Marx acquisition.

Return on Shareholders' Equity

*Excludes extraordinary item

Return on Shareholders' Equity The Company recognizes that return on investment goals must be basically long-term in nature and that the results of new investments are often unfavorable in terms of short-run earnings. Overall, however, Quaker expects that its diversified business should be able to support a regular flow of substantial new investments on which long-term returns are favorable. This concept is reflected in the accompanying table, which shows the after-tax return on shareholders' equity during each of the past five years.

Auditors' Report

To the Shareholders of
The Quaker Oats Company:

We have examined the consolidated balance sheet of The Quaker Oats Company (a New Jersey corporation) and subsidiaries as of June 30, 1971, and June 30, 1972, and the related consolidated statements of income and reinvested earnings and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of The Quaker Oats Company and subsidiaries as of June 30, 1971, and June 30, 1972, and the results of their operations and the changes in financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied during the periods.

Arthur Andersen & Co.

Chicago, Illinois,
August 25, 1972

Consolidated Balance Sheet

Assets	Thousands of Dollars	
	June 30	
	1972	1971
Current Assets:		
Cash	**$ 7,187**	$ 9,699
Marketable securities, at cost which approximates market	**15,326**	25,068
Receivables (less allowances of $2,595,000 and $1,718,000, respectively)	**89,054**	62,387
Inventories, at the lower of cost or market	**121,258**	86,546
Prepaid expenses	**5,987**	8,067
Current assets	**238,812**	191,767
Other Receivables and Investments	**5,382**	3,823
Property, Plant and Equipment, at cost:		
Land	**7,032**	6,279
Buildings and improvements	**99,842**	88,993
Machinery and equipment	**232,414**	198,407
	339,288	293,679
Less accumulated depreciation (including reserve for estimated losses on plant dispositions of $4,020,000 and $9,134,000, respectively)	**98,294**	95,208
Properties (net)	**240,994**	198,471
Intangible Assets:		
Excess of cost over net assets of acquired businesses	**27,747**	26,389
Patents, trademarks, designs, etc., less amortization	**7,751**	3,287
	$520,686	$423,737

See accompanying notes to financial statements.

Liabilities	Thousands of Dollars	
	June 30	
	1972	1971
Current Liabilities:		
Notes payable to banks	**$ 12,058**	$ 18,880
Commercial paper	**21,550**	—
Current maturities of long-term debt	**4,136**	2,390
Accounts payable and accrued expenses	**65,402**	52,050
Income taxes payable	**4,520**	6,690
Dividends payable	**3,449**	3,287
Current liabilities	**111,115**	83,297
Long-term Debt, less current maturities:		
Revolving credit notes, due 1979	**37,000**	—
3½% notes, $2,000,000 due annually to 1977	**8,000**	10,000
6½% note, $1,250,000 due annually from 1975 to 1994	**25,000**	25,000
7.70% sinking fund debentures, $1,800,000 due annually from 1977 to 2001	**50,000**	50,000
Obligations of foreign subsidiaries	**9,621**	10,294
Long-term debt	**129,621**	95,294
Other Liabilities	**2,270**	—
Deferred Income Taxes	**22,548**	15,404
Shareholders' Equity:		
Preferred, $50 par value, $3 cumulative convertible, authorized 164,631 shares; issued 158,899 and 163,199 shares, respectively	**7,945**	8,160
Common, $5 par value, authorized 22,500,000 shares; issued 12,996,209 and 12,878,007 shares, respectively	**64,981**	64,390
Additional paid-in capital	**4,993**	1,710
Reinvested earnings	**183,559**	162,805
	261,478	237,065
Less treasury common stock, at cost	**6,346**	7,323
Shareholders' equity	**255,132**	229,742
	$520,686	$423,737

Consolidated Statement of Income and Reinvested Earnings

Year ended June 30	1972	1971
	Thousands of Dollars	
Revenues:		
Net sales	**$771,159**	$678,732
Other income — net	**1,702**	1,152
	772,861	679,884
Costs and Expenses:		
Cost of goods sold	**526,974**	463,420
Selling, general and administrative expenses	**170,146**	151,267
Interest expense	**7,951**	6,556
	705,071	621,243
Income Before Income Taxes	**67,790**	58,641
Provision for income taxes	**33,546**	28,576
Income Before Extraordinary Item	**34,244**	30,065
Extraordinary (charge) credit (net of income taxes)	—	(5,886)
Net Income	**34,244**	24,179
Reinvested Earnings		
Dividends: Preferred stock	**484**	490
Common stock	**13,006**	12,636
Earnings reinvested during the year	**20,754**	11,053
Balance at beginning of year	**162,805**	151,752
Transfer to common stock re stock split	—	—
Excess of cost over par value of treasury preferred stock retired (95,489 shares)	—	—
Balance at end of year	**$183,559**	$162,805
Per Common Share: (A)		
Income Before Extraordinary Item	**$ 2.65**	$ 2.34
Extraordinary (charge) credit	—	(.47)
Net income	**$ 2.65**	$ 1.87
Dividends declared	**$ 1.02**	$ 1.00

(A) Adjusted for stock splits.

See accompanying notes to financial statements.

1970	1969	1968	1967	1966	1965	1964
597,652	$553,879	$547,194	$555,133	$498,358	$461,288	$433,461
2,745	2,738	956	881	432	519	103
600,397	556,617	548,150	556,014	498,790	461,807	433,564
399,426	375,661	382,419	403,010	358,178	328,287	316,971
140,986	128,949	121,565	114,397	103,048	99,347	84,582
4,433	2,083	2,315	2,417	1,950	1,462	1,291
544,845	506,693	506,299	519,824	463,176	429,096	402,844
55,552	49,924	41,851	36,190	35,614	32,711	30,720
27,409	24,218	20,528	17,408	18,042	16,400	16,499
28,143	25,706	21,323	18,782	17,572	16,311	14,221
—	(1,092)	—	898	—	—	—
28,143	24,614	21,323	19,680	17,572	16,311	14,221
490	495	507	528	568	581	612
11,737	10,704	9,710	8,868	8,864	8,822	8,807
15,916	13,415	11,106	10,284	8,140	6,908	4,802
139,567	129,996	118,890	108,606	100,466	93,558	88,756
(3,731)	—	—	—	—	—	—
—	(3,844)	—	—	—	—	—
151,752	$139,567	$129,996	$118,890	$108,606	$100,466	$ 93,558
2.21	$ 2.04	$ 1.72	$ 1.51	$ 1.41	$ 1.31	$ 1.13
—	(.09)	—	.07	—	—	—
2.21	$ 1.95	$ 1.72	$ 1.58	$ 1.41	$ 1.31	$ 1.13
.94	$ .87	$ .80	$ .73	$ .73	$ .73	$ .73

Consolidated Statement of Changes in Financial Position

	Thousands of Dolla	
Year Ended June 30	**1972**	197
Sources of Working Capital:		
Operations:		
Income before extraordinary charge	**$34,244**	$30,06
Depreciation and amortization	**15,393**	12,31
Deferred income taxes	**6,144**	3,07
Total from operations	**55,781**	45,45
Extraordinary charge (portion of total provision of $5,886,000 for losses from plant closings requiring current use of working capital)	**—**	(90
Sale of 7.70% debentures	**—**	50,00
Proceeds from revolving credit notes	**37,000**	-
(Decrease) in other long-term debt — net	**(2,941)**	(22,65
Sales of properties	**1,926**	2,52
Common stock issued pursuant to options and conversions	**4,337**	2,16
Other — net	**(226)**	(20
Total provided	**95,877**	76,37
Uses of Working Capital:		
Additions to properties	**40,907**	38,98
Cash dividends declared	**13,490**	13,12
Excess of cost over working capital of acquired businesses	**22,253**	5,69
Total used	**76,650**	57,80
Increase (Decrease) in Working Capital	**$19,227**	$18,56
Consisting of:		
Cash and marketable securities	**$(12,254)**	$(8,28
Receivables	**26,667**	8,20
Inventories	**34,712**	7,12
Prepaid expenses	**(2,080)**	4,33
Notes payable to banks	**6,822**	5,88
Commercial paper	**(21,550)**	-
Current maturities of long-term debt	**(1,746)**	8,68
Other liabilities	**(11,344)**	(7,39
Net increase	**$19,227**	$18,56

See accompanying notes to financial statements.

Notes to Financial Statements

Summary of Accounting Policies

Consolidation The consolidated financial statements include The Quaker Oats Company and all subsidiaries. Investments in 20% to 50% owned companies are stated on the equity basis. All significant intercompany accounts and transactions are eliminated.

Foreign currency items are translated into U.S. dollars at year end exchange rates for assets and liabilities and average annual exchange rates for income items, except property, plant and equipment and related depreciation, which are translated at rates in effect at time of acquisition.

Intangibles Excess of cost over net assets of acquired businesses represents the amount paid in excess of the fair values of the net assets of such businesses. Such costs are considered to represent continuing values and are reduced if diminution of continuing values of underlying businesses is indicated. As required by current accounting rules, any such costs resulting from acquisitions after October 31, 1970, are amortized over periods not in excess of 40 years.

Costs incurred in acquiring or developing patents, trademarks, designs, etc., are amortized on a straight-line basis over their estimated useful lives.

Inventories Inventories are based upon physical quantities priced at the lower of cost (first-in, first-out for toys and recreational products and principally average annual cost for other products) or market.

Depreciation and Properties Depreciation is provided in the accounts on the straight-line method over estimated useful lives of the properties. For tax purposes, depreciation is provided on the basis of accelerated rates as provided by applicable laws and regulations. At the present time, depreciation for tax purposes exceeds straight-line depreciation and deferred tax liability is provided for the related taxes.

The composite method is used for depreciation, and only abnormal gains and losses on sales or abandonments of property are included in income.

Research and Development Research and development costs are generally expensed as incurred.

Tax Credits The reduction in Federal income taxes in 1972 and subsequent years resulting from the job development investment tax credit for investments in new property and equipment is being deferred and amortized over the estimated useful lives of the related assets. Similar reductions from investment tax credits in prior years were reflected in income on the flow through basis.

Pension Plans The provision charged to earnings each year is sufficient to cover normal costs of the plans of the Company and its subsidiaries and, for the principal plans, amortization of prior service cost over 40 years or less.

Foreign Investments

The balance sheet at June 30, 1972 includes net assets of companies located in Canada ($14,839,000), Europe ($27,160,000) and Latin America and Pacific ($16,044,000).

Acquisitions

Louis Marx & Co., Inc., a toy manufacturer, was acquired June 30, 1972 for $51,346,000 in a purchase transaction. Its assets and liabilities as of June 30, 1972 are included in the accompanying consolidated balance sheet and its results of operations will be included in the consolidated statement

of income beginning in 1973. The $15,067,000 excess of cost over net assets acquired has been allocated to property, plant and equipment and patents, trademarks, designs, etc., at fair values, based on independent appraisals.

Needlecraft Corporation of America, Inc., a manufacturer and distributor of yarns, needlecraft kits, etc., with net assets of approximately $4,500,000, was acquired July 20, 1972, by issuance of 424,813 shares of the Company's common stock, in a merger transaction accounted for as a pooling of interests.

Pro forma operating results for 1972 and 1971 of the Company and Marx and Needlecraft based in part on unaudited data for Marx, and after adjustments for estimated additional depreciation and amortization and interest on debt (all applicable to Marx) are as follows (not covered by accompanying auditors' report):

	Thousands of Dollars	
	1972	1971
Sales	**$863,437**	$763,545
Net income (before extraordinary item in 1971)	**$ 36,423**	$ 31,605
Net income per common share (before extraordinary item in 1971) based on shares including those issued in Needlecraft merger	**$ 2.73**	$ 2.38

The Company also acquired in November 1971, Luv Pet Foods Pty. Limited (an Australian pet food manufacturer) and in July 1972, Steinmeier & Co.N.V. (a Dutch toy manufacturer) for approximately $1,300,000 cash, in purchase transactions. Results of operations of these businesses (which are not material) are or will be included in the consolidated statement of income from dates of acquisition. The related excess of cost over fair value of net assets acquired of approximately $1,276,000 is being amortized over 40 years.

Excess of Cost Over Net Assets of Acquired Businesses

Excess of cost over net assets of acquired businesses includes $26,488,000 related to acquisitions prior to October 31, 1970 (principally Fisher-Price Toys), which is not being amortized. The balance, relating to acquisitions after that date, is being amortized over periods not exceeding 40 years.

Shareholders' Equity

Stock Options On November 17, 1971, the shareholders of the Company approved the Company's 1971 stock option plan under which options covering up to 600,000 shares of common stock may be granted at not less than fair market value at the date of grant. Options granted to date under this plan are exercisable over a four-year period beginning one year after the date of grant.

At June 30, 1972, 393,632 unissued shares of common stock and 676 shares of treasury common stock were reserved for issuance upon the exercise of outstanding stock options, and an additional 500,030 unissued shares were available as of that date for granting additional options. Option prices range from $12.50 to $49.69 per share. During the year ended June 30, 1972, options covering 99,970 shares were granted at $49.69 per share, options for 127,515 shares were exercised and options for 9,591 shares were terminated.

Changes in Capital Accounts Changes in Common stock, Additional paid-in capital and Treasury common stock during 1971 and 1972 are summarized as follows:

	Amounts in Thousands of Dollars (deduct)				
	Common Stock		Additional Paid-in	Treasury Common Stock	
	Shares	Amount	Capital	Shares	Amount
Balance at June 30, 1970	12,799,856	$63,999	$ 257	243,142	$8,211
Stock options exercised and conversions of preferred stock	78,151	391	1,400	(11,017)	(372)
Sale of common stock to trustee of profit sharing plan	—	—	53	(15,300)	(516)
Balance at June 30, 1971	12,878,007	64,390	1,710	216,825	7,323
Stock options exercised and conversions of preferred stock	118,202	591	3,191	(16,408)	(555)
Sale of common stock to trustee of profit sharing plan	—	—	92	(12,500)	(422)
Balance at June 30, 1972	12,996,209	$64,981	$4,993	187,917	$6,346

Other Each share of the \$3 cumulative preferred stock is convertible at the holder's option into 1.65 shares of common stock and after January 1, 1974, may be redeemed by the Company at \$58 per share. At June 30, 1972 there were 262,183 shares of common stock reserved for conversion of the \$3 cumulative preferred stock. Preference stock of 1,500,000 shares without par value is authorized but unissued.

Income per common share is based on 12,748,424 and 12,635,245 weighted average shares outstanding during 1972 and 1971, respectively. Any dilution resulting from the exercise of stock options presently outstanding and conversion of preferred stock is not significant.

Under the terms of the note agreements, \$85,537,000 of reinvested earnings as of June 30, 1972, was not available for payment of cash dividends and/or certain other distributions to preferred and common shareholders. Minimum working capital of \$75,000,000 must be maintained and consolidated current assets cannot be less than 180% of consolidated current liabilities.

Long-Term Debt

The 7.70% debentures provide that on June 15, 1977, and each year thereafter the Company shall redeem \$1,800,000 and may redeem up to an additional \$1,800,000 of debentures, both at 100% of principal amount. Debentures may be called at any time at prices decreasing from 107.7% of principal amount currently to 100% in 1996, except that until June 15, 1981, such redemption cannot be made from the proceeds of any refunding operation having an interest cost of less than 7.70% per annum.

The revolving credit-term loan agreement provides for revolving borrowings from banks of up to \$40,000,000 (at ½ of 1% above the prime rate of interest per annum) at the option of the Company until June 30, 1975. On or

before that date the Company has the option of converting all or part of the $40,000,000 to a term loan, due June 30, 1979.

Income Taxes

Provision for income taxes on income before extraordinary item consists of:

	Thousands of Dollars	
	1972	1971
Currently payable —		
Federal	**$20,497**	$20,943
Investment tax (credit)	**(56)**	(55)
Foreign	**3,647**	2,418
State	**3,314**	2,198
Deferred (related primarily to depreciation and investment tax credits)	**6,144**	3,072
	$33,546	$28,576

Investment tax credit for 1972 is being amortized over the estimated useful lives of assets acquired. In 1971 and prior years such credits were accounted for on the flow through basis. If this basis had been used in 1972, income would have been increased $895,000, or $.07 per share.

Pension Plans

Pension expense totaled $5,351,000 for 1972 and $4,809,000 for 1971 under plans of the Company and its subsidiaries. Pension expense is funded currently. Pension funds are in excess of the actuarially computed value of the vested benefits.

Litigation

In April, 1972, the Federal Trade Commission filed charges against four manufacturers of ready-to-eat cereals, including the Company, alleging that between them they share a monopoly in the business. In the opinion of the Company the charges are without merit.

Extraordinary Charge - 1971

In 1971, provision was made for estimated closing costs and losses to be incurred by the Company in closing and selling several plants. These charges aggregated $11,208,000, which after reduction for related current tax benefits of $1,167,000 and deferred tax benefits of $4,155,000 resulted in a net extraordinary charge of $5,886,000.

Chief Executive Officer

Robert D. Stuart, Jr.
President

Corporate Staff Officers

Operations and Administration

John D'Arcy, Jr.
Senior Vice President

Thomas B. Bartel
Vice President – Personnel

Sam H. Flint
Vice President – Distribution and Operations Research

Richard H. Glantz
Vice President – Operations

Royce S. Ramsland
Vice President – Purchasing

Finance and Planning

W. Fenton Guinee
Senior Vice President

Robert A. Bowen
Vice President and Controller

Richard D. Denison
Vice President and Treasurer

Richard D. Jaquith
Assistant Treasurer

Herbert E. Trenning
Assistant Treasurer

Corporate Affairs

Robert N. Thurston
Vice President

Jack T. Redwine
Vice President and General Counsel

William F. Debelak
Secretary

Louis J. Mallardi, Jr.
Assistant Secretary

Joann A. Pitcher
Assistant Secretary

Howard J. Thomas, Jr.
Assistant Secretary

Group Management

Grocery Products

Kenneth Mason
Group Vice President

Henry T. Chandler
Vice President – Sales and Distribution

Samuel T. Gentles
Vice President and General Manager – Frozen Foods

H. Edward Miskiman
President – The Quaker Oats Company of Canada Limited

Frank J. Morgan
General Manager – The Quaker Oats Company of Canada Limited

Robert O. Nesheim
Vice President – Research and Development

William D. Smithburg
Vice President and General Manager
Cereals and Mixes Division

Robert L. Johnstone
General Manager – Candy Division

Jack M. Young
Director – Marketing Services

International Grocery Products

Augustin S. Hart, Jr.
Group Vice President

Paul E. Price
General Manager

Anthony J. Dimino
Vice President – Mexico
Managing Director – Fabrica de Chocolates La Azteca, S.A. de C.V., Mexico

Ronald G. Lagden
Director – Europe
Chairman – Quaker Oats Limited, United Kingdom

Group Management

Toys and Recreational Products

Frank C. Schell, Jr.
Group Vice President

Henry H. Coords
Vice President
President – Fisher-Price Toys Division

Jack H. Asthalter
President – Louis Marx & Co., Inc.

Lowell Fixler
President – Needlecraft Division

Industrial and Institutional Products

Archibald McClure
Group Vice President

Frederick D. Montgomery
Vice President and General Manager – Restaurants

Leonard W. Steiger, Jr.
Vice President and General Manager – Chemicals Division

Alan R. Ryan
General Manager – Burry and Institutional Products

Directors

Silas S. Cathcart
Chairman, Illinois Tool Works, Inc., Chicago, Illinois

***John D'Arcy, Jr.**
Senior Vice President – Operations and Administration

***W. Fenton Guinee**
Senior Vice President – Finance and Planning

Richard D. Harrison
President and Chief Executive Officer
The Fleming Companies, Inc., Oklahoma City, Oklahoma

***Augustin S. Hart, Jr.**
Group Vice President – International Grocery Products

Dr. James H. Hilton
Former President, Iowa State University

Dr. Lawrence A. Kimpton
Former Vice President and Director
Standard Oil Company (Indiana)

***Kenneth Mason**
Group Vice President – Grocery Products

***Archibald McClure**
Group Vice President – Industrial and Institutional Products

Donald E. Meads
Executive Vice President and Director, INA Corporation
Philadelphia, Pennsylvania

Mrs. G. G. Michelson
Senior Vice President, R. H. Macy and Company, New York

Merrill E. Olsen
Former Vice President and General Counsel

Dr. Walter J. Salmon
S. S. Kresge Professor of Marketing, Harvard Business Schoo
Boston, Massachusetts

***Frank C. Schell, Jr.**
Group Vice President – Toys and Recreational Products

Gilbert H. Scribner, Jr.
President, Scribner & Co., Chicago, Illinois

***Robert D. Stuart, Jr.**
President and Chief Executive Officer

***Robert N. Thurston**
Vice President – Corporate Affairs

Arthur M. Wood
President, Sears, Roebuck and Co., Chicago, Illinois

*Members of the Executive Committee

Corporate Headquarters
Merchandise Mart Plaza, Chicago, Illinois 60654

Transfer Agents and Registrars
The First National Bank of Chicago
One First National Plaza, Chicago, Illinois 60670

The Chase Manhattan Bank
One Chase Manhattan Plaza, New York, New York 10015

Dividend Disbursing Agent
The First National Bank of Chicago

Auditors
Arthur Andersen & Co.
69 West Washington Street, Chicago, Illinois 60602

Shares Listed
New York Stock Exchange
Midwest Stock Exchange

Ticker Symbol: OAT

Annual Meeting
Shareholders are cordially invited to attend the Company's Annual Meeting, which will be held at 9 a.m., Thursday, November 16, 1972, in the Assembly Room, sixth floor, The Northern Trust Company, 50 South LaSalle Street, Chicago, Illinois. A notice of this meeting together with the form of proxy and proxy statement will be mailed to shareholders on or about September 29, 1972, at which time proxies will be solicited by management.